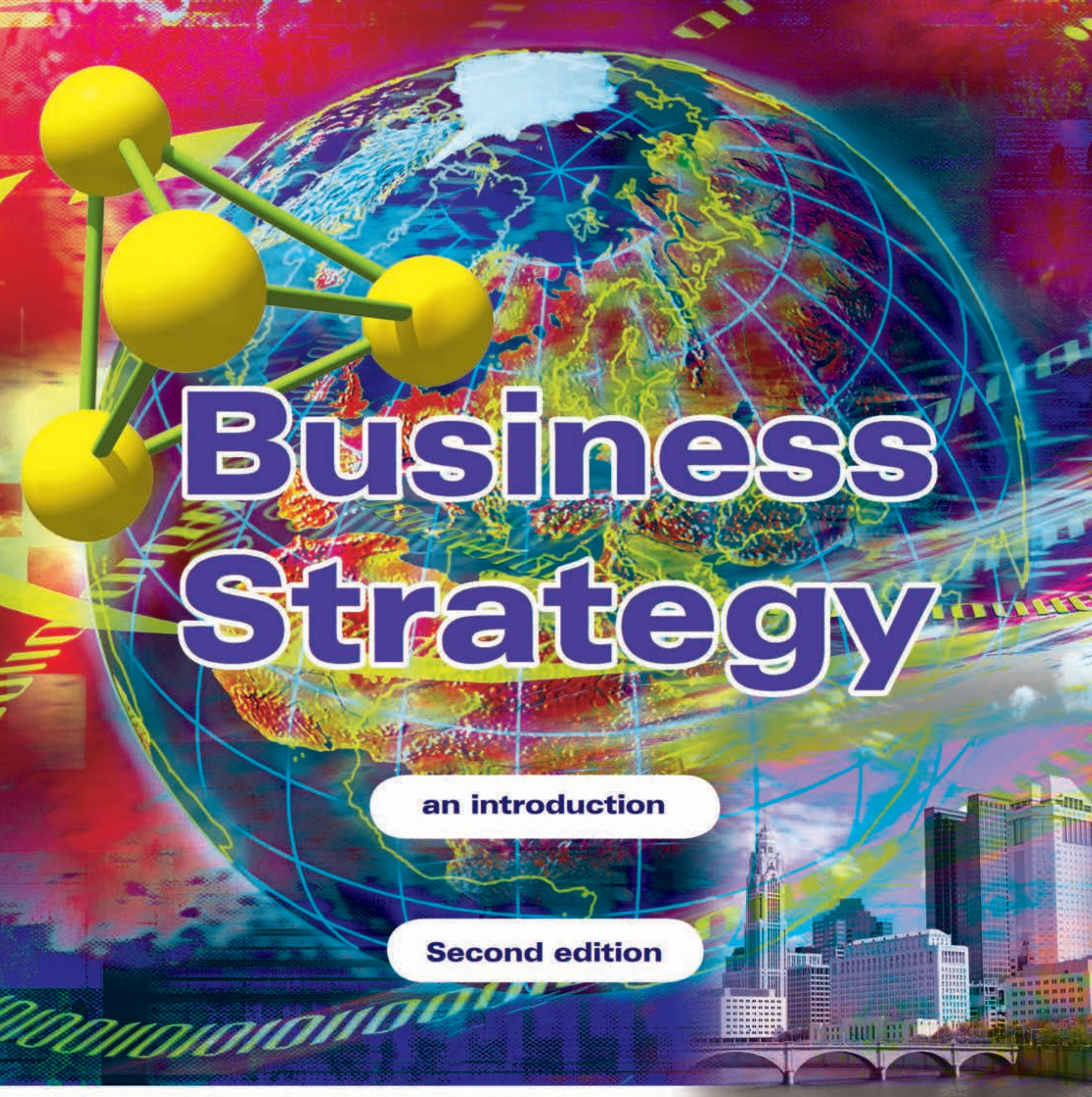

Business Strategy

an introduction

Second edition

David Campbell

George Stonehouse

Bill Houston

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Preface to the second edition

In this second edition we have attempted to retain the first edition's core qualities of accessibility, conciseness and comprehensiveness. Feedback from our many adopters, however, has enabled us to iron out a few things and add to the text in a way that will hopefully make it more useful, especially at centres with overseas students whose need for an accessible strategy text is most pronounced.

In particular, the updating has been focused in two areas. First, the suite of cases has been significantly expanded. New cases have been added and some of the existing cases have been updated. In addition to cases written by the authors, colleagues at the University of Northumbria have kindly donated a number of excellent cases to this edition. Nigel Evans wrote MyTravel (formerly Airtours plc), the outbound tour operations industry and airline alliances. Dr Colin Combe donated the case on Amazon.com. Second, we have updated the text in terms of scholarship. There is a balance to be struck between the inclusion of the most recent research and our aim to keep the text accessible to students studying strategy for the first time. The extent to which we have met this objective is perhaps a matter of opinion, but we hope that new and existing adopters will think we have got the balance about right.

Two themes in the research literature have been particularly prominent in recent years: 'knowledge management' as a source of competitive advantage in business strategy and the debate over the ethical role of businesses in society. Up-to-date scholarship on both of these themes is reflected in the second edition whilst (we hope) not detracting from the central canon of strategic management 'doctrine'. Similarly, the development of strategic perspectives other than the 'Porteresque' competitive positioning school of thought is discussed. In particular, resource dependency theory and the 'core competence' understanding of strategic management have increased in prominence in this edition.

We have been fortunate to benefit again from the experience and scholarship of two colleagues at the University of Northumbria who are seasoned experts within their respective fields. Harry Robinson updated his chapter on products and markets (Chapter 5) and Alex Appleby added the most recent scholarship to his chapter on operations and quality (Chapter 12). We thank them both for their sterling contributions to the second edition.

David Campbell
George Stonehouse
Bill Houston

University of Northumbria
May 2002

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PART I

An introduction to the strategic process

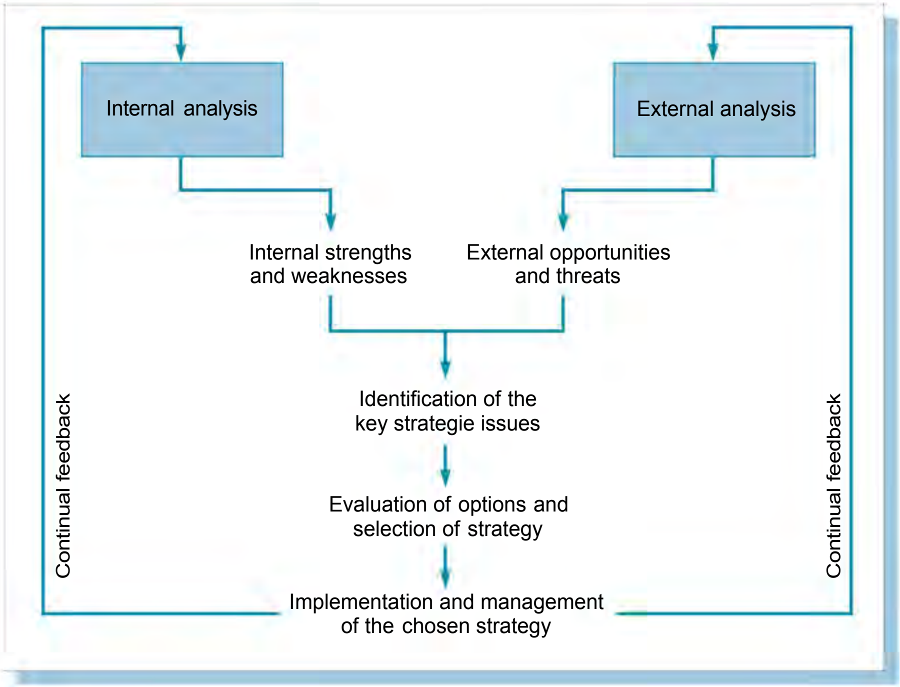
Why do we refer to business strategy as a *process*? The answer is that it is never a once for all event – it goes on and on. There is a need to continually review strategic objectives because the environment is always changing. The purpose of strategy is to make a business fit into its environment. By achieving this, the probability that it will survive and prosper are enhanced.

Furthermore, strategy is a process because it contains distinct 'stages' – three in all.

Strategic analysis

The purpose of strategic analysis is to gather information. None of us would be wise to make an important decision about anything in life without adequate and relevant information, and neither would a business.

There are two main stages in strategic analysis. Firstly, strategic analysis involves an examination of an organization's internal environment (*internal analysis*). This takes the form of a thorough analysis of the internal processes and structures of a business in much the same way as a doctor might carry out a thorough medical examination on a person. The purpose of internal analysis is to establish what the organization is good at (its strengths) and what it is not so good at (its



A schematic of the strategic process

weaknesses). We discuss the internal environment in Part II of this book.

The second stage in strategic analysis is an examination of the organization's external environment (an *external analysis*). This takes the form of a thorough analysis of two 'layers' of external environment – the micro or 'near' environment, and the macro or 'far' environment. We will encounter the external environment in Part III of the book.

The micro environment comprises the industry in which the business competes. The organization is usually affected by the factors in this environment often and it may be able to have an influence upon it. We sometimes refer to the micro environment as the competitive environment because it is within this sphere that an organization competes, both for resource inputs and to sell its product outputs. We discuss this in Chapter 7.

The macro environment contains a range of influences that affect not only an organization in an industry, but also the whole industry itself. It follows that a single organization is usually unable to affect the factors in the macro environment – successful strategy usually involves learning to cope and adapt to changes. This textbook explains the macro environment in terms of five main areas of influence – socio-demographic, political, economic, natural and technological influences. We discuss this in Chapter 6.

From the information gathered from the external analysis, we seek to establish which influences represent opportunities, and which are, or might develop into, threats. When these are considered alongside the internal strengths and weaknesses, we are able to construct a SWOT statement. A SWOT statement is a summary of the internal and external analyses. The SWOT factors are not strategies; they are observations resulting from the previous analyses.

The strengths and weaknesses are based on the internal analysis of an organization and the opportunities and threats are based on the analysis of the environment which is external to the organization. One key distinguishing characteristic between the strengths and weaknesses on the one hand and the opportunities and threats on the other is the degree of control that managers may have. With the internal strengths and weaknesses managers can often exert control whereas with regard to the opportunities and threats, managers are less likely to be able to control such factors. If for example the organization has a strong balance sheet (a strength) this will have resulted from managerial decisions. If, instead the organization is seen as being over-staffed (a weakness), managers can address the issue through reducing staff numbers. Conversely, by way of example, changing government policies, product changes by competitors or a war breaking out (all of, which might produce opportunities or threats to an individual organization depending on the circumstances) are beyond the control of managers.

The SWOT represents a position statement stating where the organization is at the time of the analysis in relation to its environment. It is not the strategy itself and should not involve making statements about what should be done next. Instead it provides a firm platform for planning for the future of the organization, i.e. formulating the strategy which is the next stage in the strategic process.

In presenting the SWOT a number of rules should be followed:

- Too much detail should be avoided so that the key points can be clearly seen. Keep each point short and to the point so that an overview can quickly be gained. The detailed justifications for the points presented in the table should be presented separately.
- Many of the points presented in the SWOT may be relative rather than absolute and consequently a matter of some judgement. Thus it is difficult to say at exactly what level a high

level of financial gearing becomes a weakness or a share of a particular market becomes a strength.

- The SWOT should not concentrate solely on ‘hard’ facts (such as financial measures or market growth statistics) that can be measured or proved. Softer factors such as organizational culture or the leadership skills exhibited by managers may be more difficult to measure but they are nevertheless important for organizational performance.
- The analysis should prioritise and combine points. The most important points should be shown first and points that are not key or strategic in nature should be excluded. In some cases it may be necessary to combine smaller points to make one large overarching point. For example, if a SWOT is partly based on a financial analysis of an organization which indicates a strong financial position, the SWOT should not have individual points on high level of profitability, low gearing, adequate liquidity, etc., for to do so would confuse the presentation. The point presented in the SWOT should be that is that the organization has a strong financial position. The justification for making such a point would be provided by the assessments relating to profitability, gearing liquidity and so on.
- The presentation should be specific, but avoid blandness, and be realistic in its assessment.

The process sometimes involves an additional stage of condensing the strengths, weaknesses, opportunities and threats (SWOT) into a survey of the ‘key issues’. These are the most pressing or most important elements of the SWOT statement – those which require the most urgent action or which the strategy should be particularly designed to address.

Once we have established the organization’s internal strengths and weaknesses, and its external opportunities and threats, the challenge becomes to select a strategy that will address the weaknesses and threats whilst at the same time, will build upon its strengths and exploit its opportunities. It is important to understand that a detailed internal and external analysis is a necessary pre-requisite for the SWOT information – it emerges from the internal and external analyses.

Strategic selection

The second stage in the strategic process involves taking the important information gathered from the strategic analysis and using it to make an intelligent and informed selection of the most appropriate course of action for the future.

It is at this stage that we come to appreciate the importance of the strategic analysis. If we have gained insufficient or flawed information from the analysis, then we cannot be sure that the strategy selection we make will be the right one.

Selection therefore begins with an examination of the strategic analysis. Once we are acquainted with it, we normally generate a list of the options open to the organization, paying particular attention to how each option will address the key issues. After this, we evaluate each option using a number of criteria. Finally, the most appropriate strategic option is selected. We discuss this matter in Chapter 9.

Strategic implementation and management

The third stage in the strategic process involves taking the selected strategic option and actually putting it into practice. We discuss this stage in Part IV of the book.

This is a rather more complex process than either analysis or selection. It involves *doing* the strategy and this brings into focus a number of other managerial issues. There are a number of areas of which we need to be aware in order to effectively implement a business strategy.

Implementation typically involves taking into account the following:

- the adequacy of the organization's resource base (Chapter 10);
- the readiness of the organization's culture and structure to undertake the proposed strategy (Chapter 10);
- the management of any changes that are needed to implement the strategy (also Chapter 10);
- deciding which, if any, growth or development paths to pursue (Chapter 11);
- the readiness of the organization's operations function to pursue the proposed strategy and any quality issues that this discussion might throw up (Chapter 12);

- the extent to which the organization positions itself in respect to its geographic coverage and international presence (Chapter 13);
- the impact that the strategy may have upon an organization's internal or external stakeholders and a discussion (if appropriate) of the strategy's implications for the organization's relationship with society (Chapter 14).

The 'feedback' link

Finally, the progress of strategy is monitored continually through feedback from the implementation stage back to the analysis stage. As a strategy proceeds, it may affect the company's internal environment and it may have an effect on the external environment. In addition, independent influences may have brought internal or external changes about since the strategic analysis was first carried out.

In order to ensure that the selected strategy is still appropriate, therefore, a review of the strategic analysis is necessary. If nothing has changed, then the company may decide that no amendment to the strategy is necessary. If the environment (internal or external) has changed, however, some modification to the strategy may become necessary.

CHAPTER

Strategy and strategic management

Introduction and chapter overview

Strategic thinking and strategic management are the most important activities undertaken by any business or public sector organization. How skilfully these activities are carried out will determine the eventual long-term success or failure of the organization. In this chapter, we introduce the most basic concepts in the study of these activities. The various definitions of the word *strategy* are discussed and then we explore the levels of decision-making in successful strategic management (at the strategic and operational levels). These are defined and the links between the levels are discussed. The different frameworks and ways of approaching strategy are introduced and then, finally, we discuss the nature of strategic objectives – who is responsible for setting them and what they are essentially about.

Learning objectives

After studying this chapter, students should be able to:

- define the word *strategy* using Mintzberg's five Ps framework;
- distinguish between deliberate (prescriptive) and emergent strategy;
- explain what strategy contains in practice;
- describe the different frameworks by which strategy is understood;

- describe what is meant by *strategic*, *tactical* and *operational* decisions;
- explain what is meant by *hierarchical congruence* and why is it important;
- explain the stakeholder model to show how strategic decisions are arrived at.

What is strategy?

Definition

At the beginning of a book on business strategy, the question 'what is strategy?' seems to be the most obvious starting point. However, the answer to the question is rather more complicated than might at first appear.

Definitions

This is because we use the word *strategy* in many ways. You may have heard people talk about a strategy for a business, a strategy for a football match, a strategy for a military campaign or a strategy for revising for a set of exams. It was this multiplicity of uses of the term that led Henry Mintzberg at the McGill University in Montreal (Mintzberg, 1987) to propose his 'five Ps' of strategy.

Mintzberg's 5 Ps

Mintzberg suggested that nobody can claim to own the word 'strategy' and that the term can legitimately be used in several ways. A strategy can be:

- a plan;
- a ploy;
- a pattern of behaviour;
- a position in respect to others;
- a perspective.

It is important not to see any of these Ps in isolation from the others. One of the problems of dividing ideas into frameworks such as the five Ps is that they are necessarily simplified. The five Ps are not mutually exclusive – i.e. it is possible for an organization to show evidence of more than one interpretation of strategy.

Plan strategies

A plan is probably the way in which most people use the word strategy. This tends to imply something that is intentionally put in train and its progress monitored from the start to a predetermined finish. Some business strategies follow this model. 'Planners' tend to produce internal documents that detail what the company will do for a period of time in the future (say five years). It might include a schedule for new product launches, acquisitions, financing (i.e. raising money), human resource changes, etc.

Ploy strategies

A ploy is generally taken to mean a short-term strategy. It tends to have very limited objectives and it may be subject to change at very short notice. One of the best examples of a ploy strategy is that employed in a football match. If the opposing team has a particularly skilful player, the team manager may use the ploy of assigning two players to mark him for the duration of the game. However, this tactic will only last for the one game – the next game will have a completely different strategy. Furthermore, the strategy will only operate for as long as the dangerous player is on the pitch. If he is substituted or gets injured, the strategy will change mid-game.

Mintzberg describes a ploy as "a manoeuvre intended to outwit an opponent or competitor" (Mintzberg *et al.*, 1998, p. 14). He points out that some companies may use ploy strategies as threats. For example, they may threaten to decrease the price of their products simply to destabilize competitors. A boss may threaten to sack an employee if a certain performance standard is not met – not because the boss intends to carry out the threat, but because he wants to effect a change in the subordinate's attitude.

Pattern strategies

A 'pattern of behaviour' strategy is one in which progress is made by adopting a consistent form of behaviour. Unlike plans and ploys, patterns 'just happen' as a result of the consistent behaviour. On a simple level, small businesses such as scrap dealers follow pattern strategies. They are unlikely to produce elaborate plans – they simply buy as much scrap metal as they can. If there is a batch of old scaffolding, then they buy it up without thinking about it. However, they would not buy old plastics because that would be outside their pattern of business behaviour. Eventually, following this consistent behaviour makes the scrap dealer a wealthy person – a successful strategy.

Such patterns of behaviour are sometimes unconscious, meaning that they do not even realize that they actually following a consistent pattern. Nevertheless, if it proves successful, it is said that the consistent behaviour has *emerged* into a success. This is in direct contrast to planning behaviour.

Key concepts

Deliberate and emergent strategy

There is a key difference between two of Mintzberg's Ps of strategy: plan and pattern. The difference is to do with the *source* of the strategy. Mintzberg drew attention to the fact that some strategies are deliberate whereas others are emergent.

Deliberate strategy (sometimes called *planned or prescriptive* strategy) is *meant* to happen. It is preconceived, premeditated and usually monitored and controlled from start to finish. It has a specific objective.

Emergent strategy has no specific objective. It does not have a preconceived route to success BUT it may be just as effective as a deliberate strategy. By following a consistent pattern of behaviour, an organization may arrive at the same position as if it had planned everything in detail.

We discuss these concepts in more detail later in this chapter.

Position strategies

A position strategy is appropriate when the most important thing to an organization is how it relates to, or is positioned with respect to, its competitors or its markets (i.e. its customers). In other words, the organization wishes to achieve or defend a certain position. We see this a lot in sport. When a new boxing champion is crowned, his only objective is to remain the champion. He wants to retain his superior position. Accordingly, all of his efforts are invested in examining his future opponents and keeping himself in shape for the next defence of the title.

In business, companies tend to seek such things as market share, profitability, superior research, reputation, etc. It is plainly obvious that not all companies are equal when one considers such criteria. Some car manufacturers have enviable reputations for reliability and quality whereas others are not so fortunate. The competitors with a reputation to defend will use a position strategy to ensure that the reputation they enjoy is maintained and strengthened. This may even include marketing messages that point out the weaknesses in competitors' products while pointing out the features of their own.

Perspective strategies

Perspective strategies are about changing the culture (the beliefs and the 'feel', the way of looking at the world) of a certain group of people – usually the members of the organization itself. Some companies want to make their employees think in a certain way, believing this to be an important way of achieving success. They may, for example, try to get all employees to think and act courteously, professionally or helpfully.

Religious groups such as the Church of England operate something approximating to this strategy. They have a number of core religious beliefs that they encourage all members to adopt. Then, it is argued, these beliefs will outwork themselves in actions. To be a good member of the Church of England, people must adopt the world view of the church. The purpose of preaching, teaching, worship and other such practices is in large part concerned with further embedding Christian beliefs into the personalities of the believers. Success is achieved when all members think in the same way – i.e. they all believe in the core doctrines and work them out in their lives through good works.

The elements of strategy

Chandler's definition

Given the foregoing definitions by Mintzberg, we might think that writers in business strategy are unable to agree to a single definition of the word strategy. This is partly true, but some have tried to sum it up succinctly to make it easier for students to understand. One such definition, still widely quoted, was offered by Professor Chandler of Harvard Business School in 1962. Given that Chandler predated Mintzberg, it is not surprising that it is rather more simplistic than Mintzberg might have accepted.

> Strategy is the *determination of the basic long-term goals* and objectives of an enterprise, and the *adoption of courses of action* and the *allocation of resources* necessary for carrying out these goals. (Chandler, 1962; emphasis added)

Three components of strategy

Chandler's is a good definition because it shows the scope of what 'good' strategy is. The italics in the above quote show the three important contents of strategy.

The *determination of the basic long-term goals* concerns the conceptualization of coherent and attainable strategic objectives. Without objectives, nothing else can happen. If you do not know where you want to go, how can you act in such a way as to get there?

The *adoption of courses of action* refers to the actions taken to arrive at the objectives that have been previously set. If your objective is to be in France, then the actions you would take would include arranging transport. You might do this by ringing travel agents, servicing your car, etc.

The *allocation of resources* refers to the fact that there is likely to be a cost associated with the actions required to achieve the objectives. If the course of action is not supported with adequate levels of resource, then the objective will not be accomplished.

Hence, strategy contains three things. In order to achieve your *objective* of being in France, you would take the *actions* of booking or arranging travel, taking leave from work and actually making the journey that will take you to France. However, the actions would not be possible if they could not be resourced. You need the *resources* of a plane, train, car or similar with a suitably qualified pilot or driver, money to pay for your travel and other such 'inputs'. If any one of these is missing, you will be unable to meet your objective.

Key concept

Resources

Resource inputs (sometimes called *factors of production*) are the inputs that are essential to the normal functioning of the organizational process. These are the inputs without which an organization simply could not continue to exist or meet its objectives. We can readily appreciate that human beings rely upon certain vital inputs such as air, water, nutrition, warmth, shelter, etc., but organizations have similar needs. An organization's resource inputs fall into four key categories:

1. *financial resources* – money for capital investment and working capital; sources include shareholders, banks, bondholders, etc.;
2. *human resources* – appropriately skilled employees to add value in operations and to support those that add value (e.g. supporting employees in marketing, accounting, personnel, etc.); sources include the labour markets for the appropriate skill levels required by the organization;
3. *physical (tangible) resources* – land, buildings (offices, warehouses, etc.), plant, equipment, stock for production, etc.; sources include estate agents, builders, trade suppliers, etc.;
4. *intellectual (intangible) resources* – inputs that cannot be seen or felt but which are essential for continuing business success, such as 'know-how', legally defensible patents and licences, brand names, registered designs, logos, 'secret' formulations and recipes, business contact networks, databases, etc.

Strategy: thinking, decisions, leadership and management

Defining the key terms

Organizations exist to serve particular purposes and to achieve related goals. Although businesses are usually concerned with providing goods and services and seeking profitability and competitive advantage over their rivals, 'not for profit organizations' such as the health service, education and charities focus on providing the best quality service with the efficient use of resources.

Earlier in this chapter, we explored some of the definitions of strategy (using Mintzberg's '5Ps' model) and we learned that there is no universally agreed definition of strategy. At the most fundamental level, an organization's strategy can be regarded as the means (plans, policies and actions) by which it seeks to achieve its long-term goal or goals. In many organizations, strategy also includes the determination of the goals and objectives themselves, as well as the means of achieving them.

Several terms are used interchangeably in the strategy literature and this can be a cause of confusion. In order to avoid confusion and to set out some of the fundamental terms used in strategy, the key terms are defined here.

Definitions

Strategic management can be viewed as a set of theories, frameworks, tools and techniques designed to explain the factors underlying the performance of organizations and to assist managers in thinking, planning and acting strategically. In simple terms, it is a vehicle through which a business can review past performance and, more importantly, determine future actions geared towards achieving and sustaining superior performance.

Strategic thinking and leadership relate to the ability of the leaders of an organization to look into its future and to think creatively about its potential development. Such thinking, vision and leadership are essential to the longer-term development of the organization. Prahalad and Hamel (1990) stressed the need for leaders to think beyond current operations so as to develop a 'strategic intent' which, they argued, shapes the organization's future strategy and development, 'stretching' it beyond its past and present achievements.

Strategic thinking is based upon strategic learning. *Strategic learning* is concerned with the processes by which leaders, managers and organizations learn about themselves, their business and environment. Strategic learning is vital to the development of the strategic knowledge upon which superior performance is based (Nonaka, 1991).

Strategic planning centres on the setting of organizational objectives, as well as developing and implementing plans designed to achieve these objectives. Rather unfortunately, strategic planning is often associated with a highly prescriptive approach to strategic management (Mintzberg, 1995). In many situations a prescriptive or deliberate approach will be inappropriate. Whilst the uncertainty of the modern business environment means that detailed and prescriptive long-term planning may be of little value, some form of broad long-term planning, related to strategic thinking and vision, is necessary if strategic intent is to be translated into action.

The debate about the 'sources' of strategy

What is the debate about?

Strategic management is a relatively young discipline and its immaturity is reflected in both the ambiguity of some of its terminology (hence the definitions above) and in the fact that there is no single agreed approach to the subject. Five distinct but often interrelated strands to strategy theory[1] can be identified:

- planned strategy (also called deliberate or prescriptive);
- competitive positioning strategy;
- core competence-based strategy (or resource-based or distinctive capability);
- emergent strategy (or learning);
- knowledge-based strategy.

Although the literature of strategic management sometimes presents these approaches as discrete and even as in conflict with each other, it is more useful to view them as interdependent and, in many ways, complementary and mutually enriching. Each approach represents a different perspective and provides analytical frameworks through which managers can gain greater understanding of the strategic capabilities of their organizations.

It is useful at this stage to consider each approach and its contribution to strategic thinking.

[1]McKiernan (1997) identified four strands to strategy theory, and the knowledge-based approach to strategy is sometimes subsumed into core competence- or resource-based strategy. We believe, however, that knowledge-based strategy has its own distinctive characteristics, at the same time as providing a fundamental underpinning for all the other theories of strategic management.

The planning approach

The prescriptive, deliberate or planned approach is based on long-term planning which seeks to achieve a 'fit' between organizational strategy and the environment in which it operates. This approach views strategic management as a highly systematized and deterministic process (Andrews, 1987; Ansoff, 1965; Argenti, 1974). The prescriptive paradigm of strategic management has been criticized as being unrealistic, particularly in times of rapid and turbulent change. Nevertheless, the need to set long-term objectives and to formulate broad plans and policies is necessary for the survival and progression of any organization. Detailed and inflexible long-term planning is, on the other hand, unnecessary and often counterproductive. Competitive advantage can be gained by being opportunistic and taking advantage of unforeseen opportunities.

The competitive positioning approach

The competitive positioning paradigm, drawing largely on the work of Porter (1980, 1985), dominated strategic management in the 1980s. It emphasized the idea of 'strategic fit' between the organization and its environment so as to achieve competitive advantage, referring to this as 'competitive positioning'. The approach is often described as 'outside-in' as the initial emphasis is on analysis of the environment before determining how to achieve a strategically desirable position. Porter's frameworks – the *five forces* (used for analysing the organization's competitive environment; see Chapter 7), *generic strategy* (used to identify sources of competitive advantage; see Chapter 8) and *the value chain* (used to analyse the activities and resources of the organization; Chapter 2) – still provide some of the most useful tools of strategic analysis. There are apparent limitations to Porter's tools but, as long as these limitations are recognized, they are valuable to managers seeking to make sense of complex organizations and their environments.

The emergent or learning approach

An alternative to the strategic planning movement is the emergent or learning approach (Lindblom, 1959; Mintzberg and Walters, 1985; Mintzberg *et al.*, 1995). This is based upon the view that the modern dynamic and hypercompetitive business environment will inevitably mean that there will be a gap between 'planned' and 'realized' or actual strategies. A rapidly changing environment means that organizations must incrementally change and adapt strategy on the basis of organizational learning. This does not preclude 'deliberate' strategic planning completely but implies that strategic plans must be flexible, guiding the overall direction of the organization, but adapted when changing circumstances dictate.

The core competence approach

In the 1990s, a strong movement developed which suggested that competitive advantage arises from an organization's internally developed *core competences* or *distinctive capabilities* rather than from its environment (Hamel and Prahalad, 1994; Heene and Sanchez, 1997; Kay, 1993; Prahalad and Hamel, 1990; Stalk *et al*., 1992). Whereas Porter (1980, 1985) stressed the importance of the industry in determining competitive advantage, this approach suggests that the core competence of the organization is of far greater importance (Baden-Fuller and Stopford, 1992; Rumelt, 1991). The approach is 'inside-out', suggesting that businesses seeking competitive advantage must first examine and develop their own distinctive resources, capabilities and competences before exploiting them in their environment. Clearly, some organizations in the same industry are more successful than others, lending support to the view that competitive advantage is largely internally developed. Equally, however, there is a danger of ignoring the environment, as customers and their needs, competitors, changes in technology, etc., can play an important role in determining competitive success.

Learning and knowledge-based strategy

What is required is an holistic view of strategy that embraces all facets of the organization (resources, capabilities, core competences and activities) and its interactions with the environment (customers, suppliers, competitors, government, legislation, technology, etc.). This holistic approach is embraced by the *learning or knowledge-based approach* to strategic management which has developed in recent years (Nonaka, 1991; Nonaka *et al*., 2000; Pemberton and Stonehouse, 2000; Stonehouse and Pemberton, 1999; Stonehouse *et al*., 2001). In essence, this approach suggests that competitive advantage depends upon the development of new and superior knowledge through the processes of organizational learning.

In fact, Prahalad and Hamel (1990) recognized the relationship between core competences, knowledge and organizational learning, defining core competences as ". . . the collective learning of the organization . . .". Later research also suggested that businesses cannot afford to be internally or externally driven. Instead, competitive advantage depends upon the ability of the organization to develop knowledge-based core competences which are essentially market-driven strategies sensitive to customer needs, based upon organizational learning (Nonaka, 1991; Nonaka *et al*., 2000; Prahalad and Hamel, 1990; Pemberton and Stonehouse, 2000; Stonehouse and Pemberton, 1999; Stonehouse *et al*., 2001). Such an approach encompasses the use of any conceptual frameworks that assist in the processes of learning and the creation of new knowledge. As Mintzberg *et al*. (1995) suggested, the various approaches to strategic management can be regarded as "complementary, representing two different forms of analysis both of which must be brought to bear for improving the quality of strategic thinking and analysis".

The approach in this book: learning and knowledge-based strategy

This book adopts an holistic approach to the subject and draws upon the theories and frameworks developed within all these perspectives. Essentially, however, competitive advantage is seen as arising from new knowledge which is, in turn, created through organizational learning. In a rapidly changing world, competitive advantage can only be sustained if the process of learning is both continuous and continual. Organizations must learn by gathering information about their business, their activities, their resources, their core competences, their customers and their needs, their competitors and other aspects of the business environment. This information must then be analysed to develop new strategic knowledge which will act as the basis of new core competences and strategies which will produce superior performance.

Strategic decisions

Different 'levels'

It is useful at this stage to understand what characterizes strategic decisions. Management decisions within any organization can be clas-

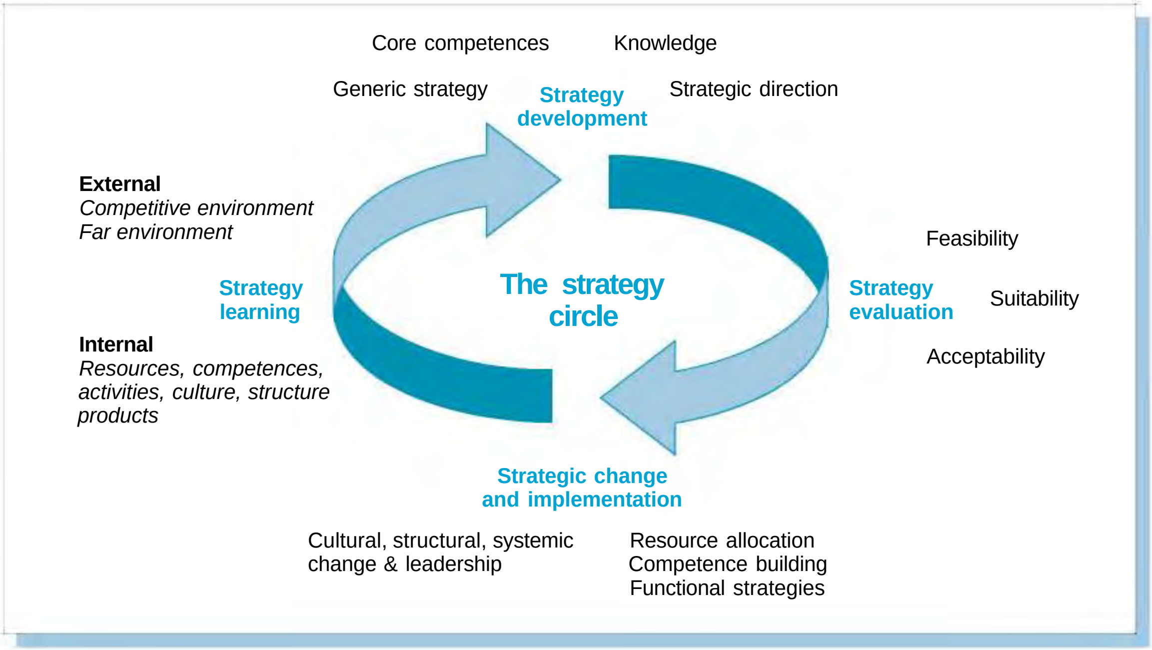


Figure 1.1
The 'strategy circle'.

sified into three broad (and sometimes overlapping) categories: strategic, tactical and operational. These can be illustrated as a hierarchy in which higher-level decisions tend to shape those at subordinate levels (see Figure 1.2).

Strategic, tactical and operational decisions within an organization differ from each other in terms of:

- focus;
- the level in the organization at which they are made;

Figure 1.2
Levels of strategic decision-making.

- scope;
- time horizon;
- degree of certainty or uncertainty;
- complexity (see Table 1.1).

The strategic level

Strategic decisions are concerned with the acquisition of sustainable competitive advantage, which involves the setting of long-term corporate objectives and the formulation, evaluation, selection and monitoring of strategies designed to achieve those objectives. Strategic decisions are made by senior managers (usually directors), they affect the whole organization, are long-term in nature, are complex and are based upon uncertain information. Managers at the strategic level require multiconceptual skills – the ability to consider the effects of multiple internal and external influences on the business and the

Table 1.1
Comparison of strategic, tactical and operational decisions

	Strategic	**Tactical**	**Operational**
Focus of decision	Achieving sustainable competitive advantage	Implementation of strategy	Day-to-day operations
Level of decision-making	Senior management, board of directors	Head of business unit or functional area	Supervisory
Scope	Whole organization	Business unit or functional area (e.g. marketing)	Department
Time horizon	Long-term (years)	Medium-term (months to years)	Short-term (days, weeks, month)
Certainty/ uncertainty	High uncertainty	Some uncertainty	High certainty
Complexity	Highly complex	Moderately complex	Comparatively simple
Examples	Decision to launch new product, enter new market, investment decision, etc.	Decision to advertise, alter price, etc.	Decision to re-order stock, scheduling of jobs

possible ways in which strategy can be adjusted to account for such influences.

The decision early on in the company's history for Easyjet to operate as a low-cost, no frills airline is an example of a strategic decision. It was taken at the most senior level, it affected the whole competitive position of the business, it was long-term in nature and it affected all members of the business.

The tactical level

Tactical decisions are concerned with how corporate objectives are to be met and how strategies are implemented. They are dependent upon overall strategy and involve its fine-tuning and adjustment. They are made at head of business unit, department or functional area level and affect only parts of the organization. They are medium-term in timescale, semi-complex and usually involve some uncertainty, but not as much as at the strategic level.

The operational level

Operational decisions are concerned with the shorter-term objectives of the business and with its day-to-day management. They are dependent upon strategy and tactics. These decisions are made at junior managerial or supervisory level, are based on a high degree of certainty and are not complex. The procedures in a sales office are typical operational activities – processing orders that have a tactical purpose in pursuit of the overall strategy.

Congruency and 'fit'

The success of strategy rests upon a very important, but rather obvious, principle. Once the strategic-level objectives have been set, the tactical and then the operational objectives must be set in such a way that they contribute to the achievement of the strategic objectives. In other words, all three levels must 'agree' or 'fit' together. This introduces the concept of *congruence*.

As shown in Figure 1.2, we can visualize the decision-making framework as a pyramid. The top, where the strategic decisions are made, is thin whereas the bottom (operational decisions) is fatter. This representation is meant to show that strategic decisions are taken infrequently whereas operational decisions are taken often. Strategic decisions are few and far between whereas operational decisions are taken weekly, daily or even hourly. For every one strategic decision, there will be more tactical decisions and possibly hundreds of individual operational decisions.

Where is a strategy actually carried out?

Although we have identified the top level in an organization's decision-making as strategic, we must not confuse this with the strategy itself, which is carried out at all levels of the organization. Strategy exists at all levels and thus it is useful to distinguish between the different levels as well as considering the relationships between them.

Network strategy

Many organizations and most businesses operate within a network of suppliers, distributors, customers and, sometimes, competitors. Although there may be no explicit strategy at this level, it is likely that the organizations will share certain objectives and information and that aspects of strategy will be devised collaboratively. Collaborative advantage through networks, strategic alliances and joint ventures can be an important source of competitive advantage. For example, collaboration between Japanese car manufacturers such as Toyota and their component suppliers, which involves the sharing of information and objectives, is at the heart of just-in-time management which, in turn, contributes significantly to Toyota's competitive edge.

Corporate strategy

Corporate strategy is at the level of the whole organization. Many organizations (especially larger ones) consist of a number of businesses which are linked together to varying degrees in terms of ownership, objectives, products, management, marketing, finance, etc. The degree of linkage can vary significantly from corporation to corporation. In terms of strategy, the degree of integration, coordination and commonality between the individual businesses can also vary enormously. It will depend upon the extent to which knowledge and core competences can be shared across the various businesses that comprise the organization. For example, Ferrari's Formula One team is heavily reliant upon the financial resources of the sports car manufacturing part of the business. At the same time, the sports car manufacturing benefits from technological developments made through Formula One racing, and the marketing effort benefits from the publicity the racing team attracts. Thus, there is a sharing of knowledge and core competences across the business and there are synergies between activities.

In some organizations, strategic decision-making takes place at the level of the business or strategic business unit (SBU). In cases where businesses within a corporation have little relationship with each other, strategic decision-making occurs largely at the level of the business or SBU. The strategic level of the organization may do little other than set broad policies and objectives, together with performance targets.

Business strategy

Much strategic decision-making takes place at the level of the business or SBU. This will be within a context set by the strategic level but which may allow considerable strategic autonomy (or not), according to whether or not there is potential for synergy and economies of scale and scope. Core competences in marketing, finance, sourcing and distribution can be shared across the whole corporation, but each business is likely to require certain distinctive competences particular to its own local geographic, competitive or industry conditions. For example, Virgin's various activities share the same brand name but different businesses demand different competences.

Functional strategy

Within the strategy of the business, each area of value-adding activity or functional area (design, procurement, production, marketing, distribution, finance, information systems, etc.) will need to design and implement a strategy that supports (i.e. is congruent with) the overall strategy of the organization. Functional strategy is of considerable importance in the successful implementation of business strategy and in its fine-tuning or tactical management.

Strategy frameworks

We have now seen that there is no single model of strategic management upon which there is general agreement. In fact, each of the strands of strategic theory makes a contribution to, and gives a complementary perspective on, how organizations achieve competitive advantage. In the same way, each strand of theory offers conceptual and analytical frameworks which assist in the process of organizational learning, strategic knowledge-building, strategic choice, strategic change and strategy implementation.

Table 1.2 summarizes some of the major analytical frameworks used in this book, their purpose and their origins.

How do businesses set strategic objectives?

Who 'owns' an organization?

Earlier in this chapter, we introduced the idea that strategic objectives, since they represent the most important level of decision-making, are set by an organization's senior management, usually the board of directors. In setting objectives, however, senior managers are sometimes influenced by a range of different groups that have an interest in the organization. Hence, a key question is: Who or what influences the senior management in their objective-setting? This question cuts to the heart of an important debate that is taking place both in universities and in business circles. This debate revolves around two different approaches towards objective-setting: the stockholder and stakeholder approaches.

The stockholder approach

The stockholder approach argues that businesses exist primarily for their owners (usually shareholders). Accordingly, any business behaviour that renders profit performance suboptimal is not only theft from shareholders but will also, eventually, lead to a level of business performance that will harm all other groups, such a employees, customers and suppliers.

In 1970, the Nobel Laureate Professor Milton Friedman contended that 'the moral obligation of business is to increase its profits'. Friedman argued that the one and only obligation of company directors (which are the legal agents of shareholders' financial interests) is to act in such a way as to maximize the financial rate of return on the owners' shares. The capitalist system upon which the Western economies are based rests in large part upon the presupposition that investments made in shares (e.g. in pension funds, unit trusts, etc.) will perform well. The profitable performance of shares lies in an increase in a share's value and in the rate of dividend per share – objectives that can only be served by financial profits. Hence, the stockholder position can usually be expressed as a 'profit maximization' dictum.

Table 1.2
A summary of analytical frameworks

Strategic process	Framework	Analytical purpose	Origin
Strategic learning: internal	Value chain	Value-adding activities	Porter – competitive positioning
	Resource	Resources	Penrose – resource-based strategy
	Core competences	Competences and core competences – competitive advantage	Prahalad and Hamel – resource/competence-based
	Products	BCG matrix	Boston Consulting Group – competitive positioning
Strategic learning: external	Five forces	Competitive environment – industry and market	Porter-competitive positioning
	Globalization drivers	Competitive environment – globalization	Yip – competitive positioning
	Strategic group	Competitive environment	Competitive positioning
	SPENT	Remote environment – social, political, economic, natural and technological (SPENT) forces	Competitive positioning
Strategy development	Knowledge – explicit and tacit	Nature of strategic knowledge	Nonaka, Stonehouse and Pemberton – knowledge-based
	Core competences	Nature and development of core competences	Prahalad and Hamel – competence-based
	Distinctive capability	Nature and development of distinctive capability	Kay – competence-based
	Generic strategy	Nature of differentiation, cost leadership and hybrid strategies	Porter – competitive positioning
	Total global strategy	Nature of global strategies	Yip – competitive positioning
Strategy evaluation	Suitability, feasibility, acceptability	Choosing appropriate strategy and direction	Competitive positioning
Strategic change and implementation	Resource allocation		Competitive positioning
	Competence-building		Competence-based
	Functional strategies		Competitive positioning
	Cultural, structural and systemic change		Organizational learning

The stakeholder approach

A stakeholder has been defined as:

> Any group or individual who can affect or [be] affected by the achievement of an organization's objectives. (Freeman, 1984, p. 46)

This definition draws in almost everybody that is, or may potentially be, involved in the life of an organization. It consequently goes without saying that not all stakeholders are equal in their influence on an organization's objectives.

The stakeholder approach (see, for example, Freeman, 1984; Donaldson and Preston, 1995) argues that organizations, like individual people, are characterized by their relationships with various groups and individuals such as employees and customers. A group or individual qualifies as a stakeholder if it has an interest in the organization's activities and has the power to affect the firm's performance and/or has a stake in it.

The implications of this proposition are far-reaching. In essence, stakeholder theory argues that shareholders are neither the sole owners of a business nor the sole beneficiaries of its activities. Although shareholders are undeniably one stakeholder group, they are far from being the only group who expect to benefit from and influence business activity and, accordingly, are just one of those groups that have a legitimate right to influence a company's strategic objectives. Some of these groups are internal to the organization whereas others are external.

Key concept

Stakeholders

A stakeholder is "any group or individual who can affect or [be] affected by the achievement of an organization's objectives". (Freeman, 1984, p. 46)

Internal stakeholders include directors, employees, employees' representatives (e.g. trades unions).

External stakeholders include shareholders, customers, suppliers, trade bodies, pressure groups, governments, competitors, local communities and 'society'.

Stakeholders and objectives

One widely used and useful model for understanding how stakeholders exert influence on an organization's objectives was proposed by Mendelow (1991). According to this model, stakeholders can be 'ranked' depending upon two variables: the stakeholder's *interest* and *power*:

- stakeholder *power* refers to the *ability* to influence the organization;
- stakeholder *interest* refers to the *willingness* to influence the organization. In other words, interest concerns the extent to which the stakeholder cares about what the organization does.

It then follows that:

$$\text{Stakeholder influence} = \text{power} \times \text{interest}$$

The actual influence that a stakeholder has will depend upon where the stakeholder is positioned with respect to ability to influence and willingness to influence. A stakeholder with both high power and high interest will be more influential than one with low power and low interest. We can map stakeholders by showing the two variables on a grid comprising two intersecting continua (Figure 1.3).

Once constructed, we can use the map to assess two things:

1. which stakeholder is likely to exert the most influence upon the organization's objectives;
2. the stakeholders that are most likely to be in potential conflict over strategic objectives (where two or more stakeholders are in close proximity in the high power–high interest part of the map).

The managing director and the board of directors are usually examples of stakeholders with both high power and high interest. This is because they not only manage the business but also depend upon it for their jobs and potential career advancement. The pub to which employees retire after or during the day's work is an example of a stakeholder with potentially high interest but low power (and therefore low total influence).

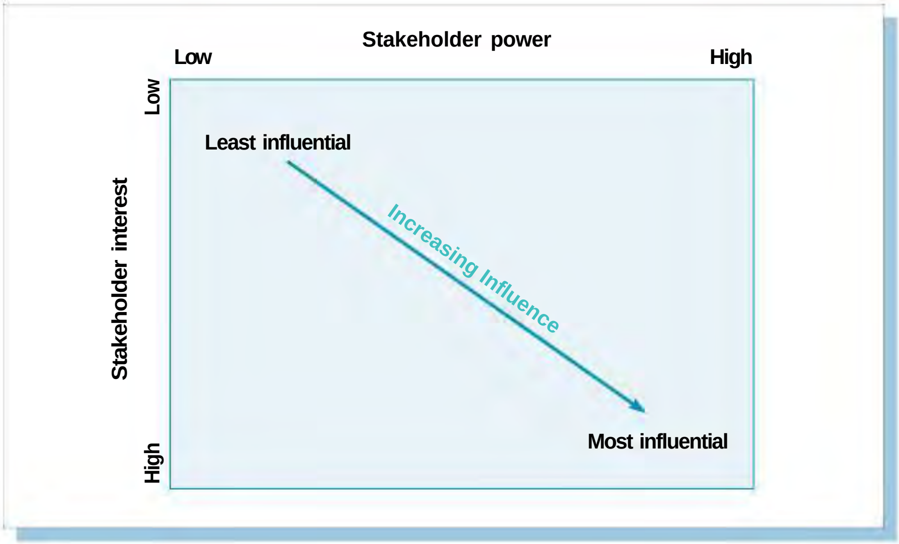


Figure 1.3 The stakeholder map (adapted from Mendelow, 1991).

Once the stakeholder map has been constructed for an organization, the competing agendas can be analysed. If, for example, two highly influential stakeholders (i.e. in the high–high quadrant) agree on corporate objectives, the momentum behind the agreed objective will be very strong. If, conversely, influential stakeholders disagree on objectives, the possibility of damaging conflict will be high. It is also important to bear in mind that the shape of the 'map' can change with time as stakeholders vary in their power and interest. A certain event, for example, might stimulate interest and push a powerful but not-as-yet-interested stakeholder into the highly influential quadrant. Similarly, high interest but low power stakeholders can sometimes increase their power by forming a joint campaign or coalition, thus moving them nearer to the high–high quadrant. The more stakeholders there are with influence, the more complex a scenario becomes when it comes to agreeing objectives.

References and further reading

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